Michael K. Jeanes, Clerk of Court
*** Filed ***
11/22/2011 8:00 AM

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2011-018944 11/18/2011

HONORABLE J. RICHARD GAMA

CLERK OF THE COURT
D. Harding
Deputy

STATE OF ARIZONA, et al. LYNETTE EVANS

v.

P M I MORTGAGE INSURANCE CO, et al. WILLIAM J MALEDON

MARY GRACE MCNEAR

MINUTE ENTRY

The Court has had under advisement Intervenor The PMI Group, Inc.'s ("TPG") Motion to Vacate Interim Order. The Court has considered the evidence presented at the November 8, 2011 hearing. Having read and considered the briefing and having heard oral argument, the Court issues the following ruling.

I. *Procedural Background.*

Defendant PMI Mortgage Insurance Co. ("PMI") is a mortgage guaranty insurer holding a certificate of authority to transact business in the State of Arizona.[1] PMI is a subsidiary of TPG. PMI's primary policyholders are the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac") (collectively, the government sponsored entities ("GSEs")),[2] which have approximately ¾ of the $103 billion of

[1] Mortgage insurance provides loss protection to mortgage lenders and investors in the event of borrower default.
[2] The Federal Housing Finance Agency is the conservator of the GSEs.

insurance in force written by PMI as of September 30, 2011. The remaining $28 billion of PMI's insurance insures approximately 1,000 different insureds.[3]

On August 15, 2011, PMI filed with the Arizona Department of Insurance (the "Department") its statutorily required financial statement, reporting a net loss of $329 million, and net incurred losses of $574 million and net earned premiums of $227 million for the period ending June 30, 2011 (the "June 30 Statement"). Based on the June 30 Statement, the Department issued Order No. 11-112-INS (the "Supervision Order") on August 19, 2011, placing PMI under administrative supervision and ordering it to stop writing new business and to cure the cited deficiencies within 60 days (i.e., by October 18, 2011). *See* A.R.S. §§ 20-169, 20-170. PMI submitted its draft cure plan (the "Cure Plan") to the Department on September 22, 2011. The Cure Plan essentially proposed (1) a partial claim payment plan ("Partial Claim Payment Plan") under which valid claims would be paid 60% in cash and 40% by a deferred payment obligation ("DPO"), or (2) the Partial Claim Payment Plan in conjunction with formation of a new company ("Newco") that would issue new mortgage insurance policies and generate additional resources.

On October 20, 2011, the Director of the Department (the "Director") filed a Verified Petition for Order to Take Full and Exclusive Possession and Control of PMI, pursuant to A.R.S. § 20-172. The Court entered an order directing the Director to take possession and control of PMI (the "Interim Order"). The Director also filed a Verified Complaint seeking appointment of a permanent receiver for PMI. The hearing on that Complaint is set for January 10, 2012.

As the interim receiver of PMI, the Director has imposed a partial claim payment plan that pays each claim 50% in cash and 50% by DPO.

II. *Discussion.*

Premising its argument on principles of fairness and procedural due process, TPG contends that the Interim Order must be vacated because the Director did not establish exigency or irreparable harm, analogizing the Interim Order to ex parte appointment of a receiver. *See* Ariz. R. Civ. P. 66(a) (ex parte appointment of receiver upon substantial cause); *Sato v. First Nat'l Bank of Ariz.*, 12 Ariz. App. 263, 265, 469 P.2d 829, 831 (1970) (ex parte appointment of receiver permissible in extreme cases where a pressing emergency exists); *see also DeSilva v. First Comm. Bank of Am.*, 42 So. 3d 285, 289-90 (Fla. App. 2010) (immediate irreparable harm necessary to obtain ex parte receivership). In fact, TPG contends there is no such exigency or

[3] TPG contends the Department's characterization of 1,000 policyholders is misleading because the majority of these account for a very small percentage of PMI's business. According to TPG, the GSEs account for approximately 70% of PMI policies, with the five largest banks in the U.S. accounting for 10-20%.

irreparable harm because as of October 20, 2011 PMI had over $2 billion in cash and highly liquid investments sufficient to pay claims until at least December 2013.

Section 20-172(A) provides:

> The director may, upon submission of a *verified petition* stating that an insurer is in such an *unsafe or unsound condition that it is or will become unable to meet the anticipated demands of its policyholders and that the condition cannot be corrected by the procedures of §§ 20-169, 20-170 or 20-171*, obtain an order from the superior court allowing the director to immediately take possession and control of the insurer pending a hearing on the appointment of a receiver. The superior court shall immediately consider the director's petition and *shall immediately issue without notice* to the affected party such order unless the verified petition filed by the director is faulty. After the order is granted, the director shall immediately, through the attorney general, apply to the superior court for the appointment of a receiver for the insurer. If at any time the court finds that no ground for receivership exists, the receivership shall be dissolved and the director's possession terminated.

(Emphasis added.)

The statute is plain and unambiguous. It does not require the Director to make a showing of exigency or irreparable harm. Clear and unequivocal statutory language is determinative of its construction. *Janson on Behalf of Janson v. Christensen*, 167 Ariz. 470, 471, 808 P.2d 1222, 1223 (1991); *Ariz. Farm Bureau Fed'n v. Brewer,* 226 Ariz. 16, 21, 243 P.3d 619, 624 (App. 2010). In any event, to the extent procedural due process principles are implicated by the Interim Order, the Court finds that § 20-172(A) defines the parameters of these safeguards, which were met in this case by the Director's compliance therewith.[4]

First, the Director has established that PMI is in "such an unsafe or unsound condition that it is or will become unable to meet the anticipated demands of its policyholders." A.R.S. § 20-172(A). The Department had been working with PMI since the financial crisis began. Although it might have $2 billion in liquid assets available for payment of claims until December 2013, PMI is currently insolvent, with a negative policyholder surplus as of September 30, 2011 of approximately $1 billion, significantly below the statutory minimum of $1.5 million. *See* A.R.S. § 20-1542(B). PMI's losses have been trending downward since 2008, and its loss projections have been off by at least 35 percent every year for the past three years, creating substantial uncertainty about the accuracy of PMI's financial forecasts.

[4] TPG argues that procedural due process requires a pre-deprivation hearing or (i) participation by a judicial officer, (ii) a prompt post-deprivation hearing, (iii) a verified petition or affidavit containing detailed allegations based on personal knowledge, and (iv) a risk of immediate and irreparable harm. *See Mitchell v. W.T. Grant Co.,* 416 U.S. 600, 605-09 (1974); *Blazel v. Bradley*, 698 F. Supp. 756, 764 (W.D. Wis. 1988).

The Department was far from sold on PMI's Partial Claim Payment Plan, which proposed to correct PMI's insolvency by treating the DPO as surplus. In the Director's opinion, doing so was inaccurate and misleading and not in accordance with statutory accounting practices. Implementation of the Partial Claim Payment Plan required at least 30-60 days for notice and hearing, the result of which was not preordained. In the meantime, PMI was making claim payments at 100% to the detriment of approximately $1.5 billion in future claims that would receive only fractional payment.[5] Further, PMI had made no tangible progress on the development of Newco. The proposed ownership structure of Newco was tenuous and was unacceptable to the Director to the extent it provided for a 19% interest to TPG. Newco's funding remained speculative at best, with no investor commitment. Additionally, the GSEs had expressed serious doubts about Newco's viability.

Second, the Director has established that "*the condition* cannot be corrected by the procedures of §§ 20-169, 20-170 or 20-171." A.R.S. § 20-172(A) (emphasis added). PMI had been operating under the Supervision Order since August 19, 2011. *See* A.R.S. §§ 20-169, 20-170. PMI's proposed Cure Plan was unacceptable and did not correct its insolvency or its inability to meet the obligations of its policyholders. Moreover, in the Director's opinion, § 20-170 did not give her authority to direct PMI to immediately initiate a DPO. A conservatorship would not have corrected PMI's insolvency either, nor could it have been put in place before notice and a hearing. *See* A.R.S. § 20-171. In addition, a conservatorship would not provide court supervision, which the Director testified would be of benefit to PMI's policyholders given PMI's size and the billions of dollars in potential losses.

"[T]he insurance industry is affected by the public interest and [] the state, by legislation, may regulate and control it." *Fireman's Fund Ins. Co. v. Ariz. Ins. Guar. Ass'n*, 112 Ariz. 7, 9, 536 P.2d 695, 697 (1975). A summary, ex parte seizure of an insurance company in order to protect the public does not violate due process. *People ex rel. Pa. R.R. Co. v. Ill. Commerce Comm'n*, 237 N.E.2d 514, 516 (Ill. 1968); *R.I. Ins. Co. v. Downey*, 95 Cal. App. 2d 220, 235-38 (1949); *see also Sato*, 12 Ariz. App. at 265, 469 P.2d at 831 (failure to give notice is not a constitutional due process defect). "[W]here public necessity requires, there can be action *followed* by a hearing." *R.I. Ins. Co., id.* at 235-36 (emphasis in original).

Here, the Director immediately applied for appointment of a receiver. *See* A.R.S. § 20-172(A). In this regard, TPG argues the January 10, 2012 hearing on that Complaint will not afford PMI meaningful relief because it will be too little-too late.[6] *See Stewart v. Citizens Cas.*

[5] The Director estimated that PMI would pay approximately $300 million in claims over the next 40-60 days, preferencing those policyholders to the detriment of others.
[6] TPG's Chairman and CEO, Larry Stephen Smith, testified that the Interim Order potentially could trigger technical default causing TPG's obligation on $736 million in bond debt to become immediately due and payable. Further,

Co. of N.Y., 244 N.E.2d 690, 696 (N.Y. 1968); *see also Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 315 (1950); *Armstrong v. Manzo*, 380 U.S. 545, 552 (1965). However, the record reflects that TPG instigated the delay of which it now complains. During a discussion regarding scheduling in Court on October 26, 2011, the Department indicated it was ready to proceed to a receivership hearing as of that day. The Court indicated its availability on November 3, 7, and 8, 2011. *TPG* proposed a 30-40 day period of expedited discovery followed by briefing and suggested the receivership hearing be held after 60 days, agreeing to the Court's proposal of early January.

Accordingly, based on the foregoing,

IT IS ORDERED denying the Motion to Vacate Interim Order.

Dated: November 18, 2011

/ s / HONORABLE J. RICHARD GAMA

JUDICIAL OFFICER OF THE SUPERIOR COURT

the Interim Order will set PMI on a course that will end with termination or resignation of key employees, dismantling of the revenue-generating side of the business, and derailing of Newco.